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IN THE

Supreme Court of the United States

OCTOBER TERM, 1997

DAVID S. HESS, MOTORCITY OF JACKSONVILLE, LTD., AND MOTORCITY OF JACKSONVILLE, INC.,
Petitioners,

v.

FEDERAL DEPOSIT INSURANCE CORPORATION, AS RECEIVER FOR SOUTHEAST BANK, N.A., *et al.*,
Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit

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REPLY BRIEF OF PETITIONERS

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The Eleventh Circuit began its *en banc* opinion by acknowledging that there is a deep and widening circuit split on the issue presented by this case: whether FIRREA "displaced the federal common law *D'Oench* doctrine." Pet. App. 3a. Notwithstanding the Eleventh Circuit's candid recognition that its position on this issue squarely conflicts with that of other circuits, the FDIC still opposes certiorari.

Indeed, the FDIC's litigating position promotes a profoundly cynical view of the law. The FDIC is prepared aggressively to litigate the *D'Oench Duhme* doctrine in any lower court and even to obtain the Solicitor General's approval to seek *en banc* review of every loss the FDIC suffers at the Circuit Court level. Thus, the FDIC has taken the position that this fundamental issue, which potentially affects every person who does any business with a bank or savings and loan and which has consumed hundreds of pages in the Federal Supplements and Federal Reporters, is sufficiently important to warrant full-court attention of every Circuit that rules adverse to the FDIC. Yet when the issue properly comes before this Court, the FDIC makes every conceivable effort to convince the Court not to decide the question. The reason is plain. Every day of delay provides the federal government with additional leverage against numerous litigants in the lower courts, who continue to feel the intense pressure of *D'Oench Duhme* to settle their claims against failed institutions on terms favorable to the federal government or its assignees. The government's litigating strategy simply belies its avowed view that "the government prevails when justice is done." The proper application of that principle in this case requires the Court to grant the petition.

The government essentially parades out the exact same arguments it unsuccessfully deployed the last time petitioners sought certiorari. Those arguments did not succeed then; the Court unanimously GVR'd in light of *Atherton* v. *FDIC*, 117 S.

Ct. 666 (1997). See *Hess* v. *FDIC*, 117 S. Ct. 760 (1997). And the arguments should fare no better now. Instead, the Court should set the case for plenary consideration and decide once and for all whether the evolving *D'Oench Duhme* doctrine remains viable in 1998 as the *en banc* Eleventh Circuit held or whether that hoary federal common law doctrine has expired as the Eighth, Ninth and D.C. Circuits have declared.

I. THE DECISION BELOW EXPRESSLY AND SQUARELY CONFLICTS WITH THE DECISIONS OF THE DISTRICT OF COLUMBIA AND THE EIGHTH AND NINTH CIRCUITS.

The FDIC concedes, as it must, that there is a conflict in the circuits on the issue presented by petitioners (Opp. 6). Nevertheless, the FDIC opposes certiorari on the ground that the conflict is not really implicated in this case because "[t]he relevant statutory provisions added or amended by FIRREA . . . do not govern transactions that occurred before they were enacted" and "[a]ll of the events giving rise to the underlying state-law claims that petitioners seek to pursue in this case took place before the enactment of FIRREA in August 1989." Opp. 6-7. Petitioners addressed this argument in their Petition (Pet. 20-21), and explained that this Court has long recognized that, in the area of federal common law, an intervening statute preempts the common law rule immediately. See *City of Milwaukee* v. *Illinois*, 451 U.S. 304, 309-10 (1981); *Murphy* v. *FDIC*, 61 F.3d 34, 40 (D.C. Cir. 1995). The FDIC makes no attempt to rebut petitioners' analysis.

The FDIC's silence is mystifying because the *City of Milwaukee* rule is of fundamental importance, not a matter of mere convenience. To ignore what Congress has said in

response to a problem and to adopt a contrary rule as a matter of federal common law is simply inconsistent with a federal court's "commitment to the separation of powers . . . " *Murphy*, 61 F.3d at 40 (quoting *City of Milwaukee*, 451 U.S. at 315). Thus, the relevant inquiry is whether a federal court today is permitted to continue to tap into a "vast" and "evolving" common law in light of Congress's specific guidance on the issue presented in this case. That question is squarely posed in this case. Accordingly, the FDIC's retroactivity argument provides no basis to deny certiorari.[1]

Ultimately, the makeweight nature of the retroactivity argument is demonstrated by the fact that it wholly ignores the scope of the Eleventh Circuit's holding in this case. The FDIC

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[1] In any event, even if retroactivity were the relevant inquiry, the FDIC's position ignores 12 U.S.C. § 1821(d)(2)(H), which provides that all post-FIRREA *receivers* "*shall* pay all valid obligations of the insured depository institution in accordance with the prescriptions and limitations of this chapter." (emphasis added). This provision makes clear that Congress intended for the FDIC's protections to be limited to statutory defenses as of the date of enactment. *See* Pet. 21 n.12. To permit the FDIC to avoid liability to petitioners in 1998 does complete violence to the plain language of 12 U.S.C. § 1821(d)(2)(H).

Moreover, the FDIC's assumption that the date of the loan agreement is the relevant date for retroactivity purposes is doubtful. In *O'Melveny & Myers* v. *FDIC*, 512 U.S. 79, 87 (1994), this Court indicated that the date of the receivership (in this case, two years *after* the enactment of FIRREA) would be relevant. In addition, it would be anomalous, at best, to use the date of the loan agreement as the trigger for determining whether petitioners' rights are governed by FIRREA or by federal common law. At the time of the loan agreement in this case, petitioners simply entered into a contract with a solvent bank and could not have anticipated that their rights in the event of a breach would be governed by federal law at all or that they would have to litigate against the FDIC.

raised the retroactivity issue below and the court dismissed it as irrelevant because FIRREA did not displace the *D'Oench* doctrine:

> Finally, the FDIC has argued for the first time on remand that FIRREA cannot apply to this case because the alleged arrangement at issue occurred prior to FIRREA's enactment. . . . *Because we conclude that FIRREA did not displace the D'Oench doctrine*, and because we conclude that Motorcity's claims are *D'Oench*-barred, we need not delve into an analysis of whether FIRREA's application to this case would pose a retroactivity problem.

Pet. App. 10a n.6 (emphasis added). This language makes crystal clear that the Eleventh Circuit intends to apply the *D'Oench* doctrine to all claims -- both pre-FIRREA claims and post-FIRREA claims.

Indeed, the Eleventh Circuit's broad application of the *D'Oench* doctrine is demonstrated in *First Union Nat'l Bank* v. *Hall*, 123 F.3d 1374 (11th Cir. 1997), petition for cert. filed, 66 U.S.L.W. 3532 (U.S. Jan. 28, 1998) (No. 97-1296), which the FDIC largely ignores in its Opposition (Opp. 10 n.7). In *Hall*, a panel of the Eleventh Circuit applied the federal common law *D'Oench* doctrine to bar a counterclaim involving a specific asset of a bank, which had acquired the asset from the FDIC. *Hall* involved a pre-FIRREA loan agreement, but other events, such as the conduct that gave rise to the counterclaim, took place after FIRREA was enacted. The court of appeals, however, did not address any issue of timing or any other factual differences in holding that the *D'Oench* doctrine applied; it simply relied on the decision in this case. 123 F.3d at 1379.

Thus, *Hall* removes any doubt that the Eleventh Circuit broadly applies the *D'Oench* doctrine to protect the FDIC and its private successors-in-interest, regardless of whether the underlying transaction involves a specific asset of the bank and regardless of whether the relevant events took place before or after the enactment of FIRREA. Accordingly, the acknowledged circuit split is squarely raised in this case.

II. THE COURT SHOULD GRANT THE PETITION TO DECIDE THE PROPER RELATIONSHIP BETWEEN *UNITED STATES* V. *TEXAS*, AND *O'MELVENY* AND *CITY OF MILWAUKEE*.

Petitioners demonstrated that an independent ground for granting review in this case is that the decision below suggests that there is a lack of clarity in this Court's decisions concerning the relationship between federal common law and federal statutes. In particular, the relationship between this Court's decisions in *United States* v. *Texas*, 507 U.S. 529 (1993), *O'Melveny & Myers* v. *FDIC*, 512 U.S. 79 (1994), and the line of cases including *City of Milwaukee* v. *Illinois*, 451 U.S. 304 (1981), has at least confused the Eleventh Circuit. Pet. 22-28.

The FDIC's only response to this argument is a conclusory footnote arguing that there is no such confusion because the difference is that *Texas* involves "determining whether a new statute should be deemed to abrogate *old* common law, while cases like *O'Melveny* (and *Atherton*) involve determining whether it would be appropriate under particular circumstances to create *new* common law." Opp. 9 n.6.

The FDIC does not cite any authority for this "distinction," and no such authority exists. To the contrary, this Court has

made clear that "old" federal common law cannot survive once Congress legislates in an area. *Murphy*, 61 F.3d at 40. When Congress enacts a comprehensive statute that addresses a particular subject, the statute "preempts" not only existing federal common law rules, but the entire field of judicial lawmaking as well. As this Court stated in *Northwest Airlines, Inc.* v. *Transport Workers Union*, 451 U.S. 77, 95 n.34 (1981), "once Congress addresses a subject, even a subject previously governed by federal common law, the justification for lawmaking by the federal courts is greatly diminished. Thereafter, the task of the federal courts is to interpret and apply statutory law, not to create common law." Indeed, this Court has said that the need for federal courts to develop common law "disappears" once Congress enters a field. *City of Milwaukee* v. *Illinois*, 451 U.S. 304, 314 (1981) ("[W]hen Congress addresses a question previously governed by a decision rested on federal common law the need for such an unusual exercise of law-making by federal courts disappears").

Moreover, even if federal courts could continue to apply a very specific federal common law rule after Congress has enacted a comprehensive statute, the FDIC's distinction between "old" common law and "new" common law is untenable. The Eleventh Circuit did not apply the rule of *D'Oench*. That rule is codified in 12 U.S.C. § 1823(e)(1). Instead, what the court of appeals applied was its vision of an ever-expanding *D'Oench* doctrine. In its first decision in this case, the *en banc* court described the common law *D'Oench* doctrine as "vast" and, more significantly, "evolving." No. 96-106 Pet. App. 24a-25a (emphasis added). Following remand, that court reinstated its prior decision, reaffirming its conclusion that Congress "intended to continue the harmonious, forty-year coexistence of the statute and the *D'Oench* doctrine." Pet. App.

8a. Even though the court purported to distinguish *O'Melveny* and *Atherton* on the ground that those decisions addressed the issue of *creating* federal common law, Pet. App. 6a, the court of appeals did not establish any limit on its ability to apply the "vast" and "evolving" *D'Oench* doctrine.

In sum, the notion that there is a difference between creating a "new" common law rule after Congress has acted (which both sides agree is prohibited) and expanding an "old" common law rule (which the 11th Circuit and the FDIC apparently believe is permissible) means simply that the seemingly narrow rule of *United States* v. *Texas* swallows the much more sweeping principles of *City of Milwaukee* and its progeny. Perhaps the Court is prepared to cut back as violently on the latter doctrine as the FDIC proposes, even though the rule embodies core separation of powers principles, but at a minimum the issue warrants this Court's immediate review.

III. THE QUESTION PRESENTED IS AN IMPORTANT AND RECURRING ISSUE IN THE FEDERAL COURTS.

Petitioners demonstrated that the question of the viability of a federal common-law *D'Oench* doctrine is an important and recurring issue that arises in several federal court cases each month. Pet. 19.

The FDIC contends that this question does not warrant review because (1) cases involving so-called "pre-FIRREA" transactions are "of little continuing importance" since they "comprise a finite set that is rapidly diminishing over time"; and (2) cases involving so-called "post-FIRREA" transactions will not arise because "the FDIC's recent policy statement makes

clear that the FDIC will not assert the common-law *D'Oench* doctrine in cases involving post-FIRREA transactions." Opp. 10. Both arguments are completely makeweight.

With respect to cases involving what the FDIC has termed "pre-FIRREA" transactions, its assertion that these cases are "of little continuing importance" is astonishing because the Solicitor General has authorized the FDIC to seek rehearing and *en banc* review in every case the FDIC has lost, including most recently, *Ledo Financial Corp.* v. *Summers*, 122 F.3d 825 (9th Cir. 1997). As the FDIC noted in its Opposition, it is seeking review in *Ledo* of the panel's "conclusion that there was no longer sufficient federal interest to apply the common law rule to pre-FIRREA transactions." Opp. 6-7 n.3. The FDIC's position in *Ledo* that the question whether the *D'Oench* doctrine applies to "pre-FIRREA" transactions is of sufficient national importance to warrant *en banc* review by the Ninth Circuit wholly undermines its position in this case that the issue has limited prospective significance. It cannot be true that the issue is important whenever the FDIC loses, but unimportant if the FDIC wins.

With respect to cases involving what the FDIC has termed "post-FIRREA" transactions, the FDIC's Statement of Policy (reprinted in Appendix to Opp.), which declares that the FDIC will not assert the *D'Oench* doctrine as a defense in certain cases, will not prevent the issue from arising in future cases. The FDIC typically transfers the assets that it acquires through receiverships to other entities, which stand in the FDIC's shoes for purposes of claims concerning those assets. These transferees are not bound by the FDIC's recent policy statement, and will continue to assert the *D'Oench* doctrine, as they have in several cases already. In *Hall*, for example, First

Union National Bank (which had acquired Mr. Hall's note), rather than the FDIC, was the party that successfully invoked the *D'Oench* doctrine against Mr. Hall. Similarly, in *DiVall Insured Income Fund Ltd. Partnership* v. *Boatmen's First Nat. Bank*, 69 F.3d 1398 (8th Cir. 1995), Boatmen's National Bank (the FDIC's successor-in-interest) unsuccessfully asserted protection under the *D'Oench* doctrine because that court held *D'Oench* was preempted for all purposes. Thus, the self-imposed "restraint" embodied in the FDIC's Statement of Policy (which could be revoked at any time) does not reduce the need for the Court to resolve the conflict in the circuits.

The FDIC also questions the significance of the over 100 reported cases since this Court decided *O'Melveny* in which the FDIC or other federal successors have relied, at least in part, on the *D'Oench* doctrine. Pet. 19 and n.10. The FDIC notes that the majority of these cases involve the question "whether new Section 1821(d)(9)(A) applies only in cases that involve an identifiable bank 'asset,'" and suggests that these should not have been counted since the claims in this case (contract and tort claims against the bank) did not involve an identifiable bank asset. Opp. 10 n.7. This argument misses the point. The question whether the *D'Oench* doctrine has survived FIRREA is implicated in both the "asset" and "no asset" cases, particularly in the Eleventh Circuit. Thus, this case is an appropriate vehicle for the resolution of that issue, and that issue is litigated every day of the year. Indeed, the fact that this is a "no asset" case arguably makes it an even better vehicle for resolution of the *D'Oench* issue because it permits the Court to reach the question whether it is sound policy to distinguish between "asset" and "no asset" cases. See Petitioners' first Petition for Certiorari, at 26-28 (No. 96-106).

* * * * *

At the end of the day, the question presented here is precisely the same as the question presented by petitioners almost two years ago. At that time the FDIC asserted identical arguments in favor of denying the petition. The Court rejected the FDIC's effort then and it should do the same today. If anything, the need for review by this Court is more acute now because the conflict among the courts of appeals has widened and deepened. Customers of banks and assignees of the FDIC both deserve a uniform rule by which to order their affairs and uniformity can only be obtained now from this Court.

CONCLUSION

For the foregoing reasons, and for those stated in the petition, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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